September 26, 2007

Mr. David Ikari, Chief
Dairy Marketing Branch
California Department of Food and Agriculture
560 J Street, Suite 150
Sacramento, CA 95814

RE: Alternative Proposal for Class 4a and 4b Hearing

Dear Mr. Ikari:

On behalf of its producer–members, California Dairies, Inc. (CDI) respectfully submits this alternative proposal in response to the Revised Notice of Public Hearing issued September 24, 2007. The hearing notice was revised by the Department of Food and Agriculture to include consideration of amendments to the Stabilization and Marketing Plans for Market Milk for the Northern and Southern California Marketing Areas, as well as the Pooling Plan for Market Milk.

Proposed Class 4a Pricing Formula

CDI proposes that the following formula for Class 4a milk be adopted:

Fat = (CME AA Butter Price -$0.0397 -$0.1607) x 1.2

SNF = (California NFDM Price - $0.1698) x 1.0

CDI's proposed changes are consistent with the objectives stated in previous hearings — the Class 4a formula should reflect the most currently available cost-justified changes. This applies to not only the manufacturing cost allowances for butter and nonfat dry milk but to the f.o.b. price adjuster for butter as well. Simply, the manufacturing cost allowances should be consistent with actual costs for processing, and the butter commodity price should adjusted by a factor that reflects what California plants actually receive for the products they produce.

ARTESIA	FRESNO	LOS BANOS	TIPTON	TURLOCK	Corporate: VISALIA
11709 E. Artesia Blvd.	755 F Street	1155 Pacheco Avenue	11894 Avenue 120	475 South Tegner	2000 N. Plaza Dr.
PO Box 6210	PO Box 11865	PO Box 2198	PO Box 837	Turlock, CA 95380	Visalia, CA 93291
Artesia, CA 90702-6210	Fresno, CA 93775-1865	Los Banos, CA 93635-2198	Tipton, CA 93272-0837		
Tel.: 562-865-1291	Tel.: 559-233-5154	Tel.: 209-826-4901	Tel.: 559-752-5200	Tel.: 209-668-6150	Tel: 559-625-2200
FAX: 562-860-8633	FAX: 559-268-5101	FAX: 209-826-6717	FAX: 559-752-5201	FAX: 209-668-6162	FAX: 559-625-5433

CDI's proposal increases the butter and nonfat dry milk manufacturing cost allowances to the weighted average of the costs incurred by CDI's own plants in 2006. CDI suggests the costs derived from its own plants are more relevant than the composite of plant costs compiled and reported in the Department's Manufacturing Cost Studies for 2006 released in September 2007. Whereas some of the other plants in the cost studies are multi-product plants, CDI's plants manufacture only butter and nonfat dry milk, making the allocation of costs, particularly overhead costs, much more transparent and more accurate.

CDI's proposal also incorporates information taken from the Department's analysis of the relationship between butter prices received by California processors and the Chicago Mercantile Exchange (CME) price for butter. CDI proposes using the weighted average difference for the 24–month period with the weighting applied to the entire 24-month period, as reported in the analysis released September 2007. This approach accounts for the month-to-month sales volume differences appropriately and uses an acceptable statistical approach to do so. As such, it is a better representative of the underlying relationship between prices received by California butter plants and CME butter prices than the figures obtained using the other methods included in the Department's analysis.

Proposed Plant Processing Capacity Credit

As has been mentioned in the past several hearings, plant processing capacity in California is approaching a critical point of imbalance relative to the milk being produced in the State. The Department has recognized the plant capacity problem but has limited tools with which to address the problem. For example, the Department has the ability to increase manufacturing cost allowances to encourage the building of new plants or the expansion of existing plants. However, such a generalized approach to encourage plant capacity has typically resulted in lower prices to dairy producers without adding any new plant processing capacity in California, i.e., increasing the manufacturing cost allowance does not assure that the money diverted from dairy producers to milk processors will be used to increase plant capacity in the State. In the view of CDI, the Department has not been given the ability to encourage specifically those companies that are considering adding new milk processing capacity to the California dairy landscape.

CDI proposes that an incentive be given to plants that add processing capacity to the state, either through a new facility or an expansion of an existing facility. In the case of an expansion of an existing facility, the credit would only apply to the expanded portion of the plant, not the entire facility. Furthermore, the credit would not apply to a plant that simply processes more milk without changing its structure or equipment.

The incentive would be in the form of a credit to the plant's pool obligation. CDI has first-hand experience with the costs of constructing a new plant, and a credit of $0.50 per cwt. is consistent with the costs of constructing a new plant. The credit is to be provided entirely on the solids not fat price and would apply to eligible plants for a period of three years.

The attached extracts from the current Stabilization and Marketing Plans for Northern California and Southern California and for the Pooling Plan for Market Milk reflect CDI's proposed amendments.

Thank you for your consideration of CDI's alternative proposal.

Sincerely,
Dr. Eric M. Erba
VP Government Relations
California Dairies, Inc.

Proposed Changes to Article III, Section 300.0 of the Stabilization and Marketing Plans for Northern California (Plan 50) and Southern California (Plan 65):

(D) The minimum prices to be paid for components used for Class 4a shall be computed as follows:

(1) For all milk fat, not less than the price per pound computed by the formula using the butter price, less an f.o.b. California price adjuster of ~~one and sixty-eight hundredths cents ($0.0168)~~ three and ninety-seven hundredths cents ($0.0397), less a manufacturing cost allowance of ~~fifteen and six- tenths cents ($0.156)~~ sixteen and seven hundredths cents ($0.1607), and the result multiplied by a yield factor of one and two–tenths (1.2).

(2) For all milk solids-not-fat, not less than the price per pound computed by the formula using the nonfat dry milk price, less a manufacturing cost allowance of ~~sixteen cents ($0.16)~~ sixteen and ninety-eight hundredths cents ($0.1698), multiplied by a yield factor of one (1.0).

Proposed Addition to Article III of the Stabilization and Marketing Plans for Northern California (Plan 50) and Southern California (Plan 65):

Section 300.5 Each handler with either Class 4a or Class 4b utilization, who has constructed a processing plant or expanded an existing plant after January 1, 2008, may deduct from the applicable minimum prices pursuant to Section 300.0 Paragraph (D) and (E) a plant capacity credit not to exceed $0.50 per cwt. The credit shall apply to all milk processed in a new plant and to only that additional milk processed as a result of the expansion of an existing plant.

Proposed Addition of Article 8.5 of the Pooling Plan for Market Milk (Order 106)

Section 850. Each handler entitled to adjustments for plant capacity increases or expansions, as set forth in Section 300.5 of the Stabilization and Marketing Plans, shall submit a report for each month which shall be postmarked no later than 45 days following the end of the month. Such report shall set forth adjustments to the handler's pool obligation as specified in this article.

Section 851. The following shall be shown for milk processed for which a plant processing capacity credit is provided for under Section 300.5 of the Stabilization and Marketing Plans:

(a) The pounds and solids-not-fat content of the market milk processed by the qualifying facility or qualifying portion of the facility as specified in Section 300.5 of the Stabilization and Marketing Plans;
(b) The computation of the plant capacity credit for market milk based on the rate specified in Section 300.5 of the Stabilization and Marketing Plans.

Section 852. The secretary shall verify and correct, if necessary, the adjustments requested under this article and adjust the handler obligation accounts within 60 days after receiving the handler report. The handler adjustments shall be reflected in the solids not fat prices by adjustment of the net pool balance utilized pursuant to Paragraph 902(c) or Section 906, whichever is applicable.

Proposed Addition to Article 9, Section 906 of the Pooling Plan for Market Milk (Order 106)

(e)(6) Subtracting the total plant capacity credit, calculated pursuant to Article 8.5.